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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945.

No. [redacted] 5

ELECTRIC POWER & LIGHT CORPORATION,

Petitioner,

against

SECURITIES AND EXCHANGE COMMISSION.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

REPLY BRIEF FOR PETITIONER ELECTRIC POWER & LIGHT CORPORATION.

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November 13, 1945.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945.

ELECTRIC POWER & LIGHT CORPORATION, Petitioner, *against* SECURITIES AND EXCHANGE COMMISSION.	No. 7

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

REPLY BRIEF FOR PETITIONER ELECTRIC POWER & LIGHT CORPORATION.

Introduction.

Basic to the position of the Commission before this Court, apart from questions of constitutional law and of the power of the Commission to dissolve holding companies, are two contentions with respect to the administration of Section 11 of the Public Utility Holding Company Act of 1935.

FIRST, the Commission is compelled to claim the right to disregard completely the status of particular holding companies and particular holding company systems under the Act whenever such holding companies and holding company systems are controlled by another holding company and are a part of another holding company system.

SECOND, the Commission is compelled to claim the right to disregard the integration requirements of Section 11(b)(1) so long as it purports to be acting under Section 11(b)(2).

Electric maintains that if either of these contentions which underlie the arguments of the Commission is erroneous, the order for the dissolution of Electric must fall. Electric also maintains that both these contentions with respect to the administration of Section 11 of the Act are entirely untenable.

In addition, despite sixteen pages of argument (Comm. Br., pp. 46-62), the findings of the Commission as to inequality of voting power, which are basic to the dissolution order, still rest upon figures which are derived from unsound guesses, assumptions and computations.

I.

The Commission's disregard of Electric's status under Section 11.

Electric set forth in its main brief the plain fact that Section 11 imposes upon the Commission certain duties with respect to *each* and *every* registered holding company and holding company system. Electric is a registered holding company, owning a holding company system, and the Act makes no distinction between one holding company and another.

It is true that Electric is a part of the Bond and Share holding company system, which did not at the time of the hearings in this proceeding comply with Section 11. However, unless Section 11 compels the Commission to dissolve all holding companies in a large and scattered holding com-

pany system, or unless Section 11 has nothing whatever to guide the Commission, the requirements of Section 11 with respect to the integration and simplification of *each* and *every* holding company and holding company system must import a duty on the part of the Commission with respect to Electric as well as with respect to Bond and Share.

The Commission comments upon these matters in the following manner:

> "Thus, while it is proper to refer to the American and Electric systems as separate holding company systems, the Bond and Share system includes both the American and Electric systems as well as the systems of other subsidiary holding companies. Likewise, the term security holders of the Bond and Share system includes holders of securities in petitioners and their operating subsidiaries as well as security holders in Bond and Share. Statements in the briefs of petitioners evidence a correct understanding of this distinction, e. g. Amer. Br., pp. 7, 17, 93, 115, Elec. Br., p. 5. Nevertheless it is elsewhere incorrectly stated that the issues included solely the effect of or position of petitioners in the Bond and Share system and not their position or effect within their own systems (Amer. Br., p. 9; Elec. Br., p. 35). *The implication is that the Commission could not consider the impact of their corporate structure and existence upon security holders of petitioners, or of petitioners' subsidiaries. This seems largely a play on words.*"* (Comm. Br., pp. 18-19).

Electric did not argue that the Commission "could not consider the impact" of Electric's corporate structure and existence upon its security holders and those of its subsidiaries. Electric argued, and the fact is, that the proceed-

* Emphasis in quotations added, unless otherwise noted.

ing was not directed to a consideration of that "impact"; nor was that the basis of the dissolution order.*

The Commission could, of course, "consider the impact" of Electric's corporate structure and existence upon its security holders and upon the security holders of its subsidiaries. But it is absurd to contend, assuming the Commission to be "considering" Electric and Electric's system, that Electric's system can be said to be simplified and integrated by dissolving Electric.

Indeed, the Commission is apparently aware of the fallacy of its position. The Commission repeatedly protests that no harm can come from the dissolution order, since the Commission may lift the order of dissolution at some future time provided Electric has meanwhile simplified and integrated itself. (Comm. Br., pp. 31, 102, 133-134).

Electric's contention, however, was that if there are conditions upon which Electric may continue to exist, responsible administration required that the Commission order those conditions to be fulfilled. That was its job. Its job was not to order dissolution and then facilitate or not, as it desires, the accomplishment of the ultimate objectives of the Act.

A reading of the Commission's brief only buttresses the conclusion reached after reading its findings and opinion, that the dissolution order is not based upon the effect of the continued existence of Electric upon its own system. The Commission's ultimate justification for the dissolution of Electric inevitably returns at every point, in its

* Indeed, at no point either in the Commission's findings and opinion, in its briefs below, in the court's opinion below, or in the Commission's brief before this Court has the case respecting Electric alone under Section 11(b)(2) been clearly stated—even without regard to the coordinate provisions of Section 11(b)(1). Facts regarding companies throughout the Bond and Share system have always been intermingled with facts respecting Electric as support for action by the Commission against Electric or conclusions respecting it.

brief as well as in its opinion, to the fact that Electric is an intermediate holding company in the Bond and Share system and is being dissolved to remedy defects in that system, not in Electric's.

The mere fact that a holding company and a holding company system are a part of another holding company system is not *per se* ground for dissolution. The insistence of the Commission that it may dissolve Electric simply because it has a "pyramiding" effect in another holding company system is in clear contravention of the provisions of Section 11 imposing the same duty upon the Commission with respect to the simplification and the integration of *each* holding company system.*

In its main brief (pp. 31-33, 43-44), Electric pointed to the severance of Bond and Share control of Electric as the remedy most closely related to the evils alleged in the Commission's findings, and as a complete and direct remedy for those evils. Electric argued that the existence of so direct and complete a remedy disclosed how arbitrary and unreasonable the dissolution of Electric is as a cure for the evils which are charged against Bond and Share.**

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* The Commission's brief (f. n., pp. 17-18) asserts that the narrowing of the issues to the sole question of whether or not Electric should be dissolved was "in response to respondents' objections". The inference that the respondents sought such a narrow issue is contrary to the fact (R., Vol. I, 57-66).

Moreover, the court below was in error in stating (R., Vol. IV, 874-n) that despite such narrowing of the issues, Electric could still present and have considered any relevant matters under Section 11(b)(2). The Commission in its June 7th order, by which the issues were narrowed, specifically reserved all other issues set forth in the order calling the hearing (R., Vol. I, 27, 50, 66). The issues reserved included everything under Section 11(b)(2) except dissolution alone.

** Incidentally, the Commission neglects to state, when it quotes at length from the Bond and Share plans of July 25, 1945 (Comm. Br., pp. 118-123), that one of the steps therein provided for is the severance of Bond and Share's control of Electric.

Nowhere in the Commission's brief does it answer the foregoing argument. It states that the severance of Bond and Share control would have presented difficulties, and the difficulty most relied on, is stated to relate.

> "to appraising the value of Bond and Share's holdings of petitioners' common stock, either for purposes of a fair and equitable plan of distribution among its stockholders or for passing on a sale price." (Comm. Br., p. 126).

Elsewhere, however, the Commission had already stated that in passing upon sales prices for securities, the Commission has limited its regulatory functions

> "to insistence upon arms' length dealings and adequate disclosure to possible purchasers, and has not prevented the vendor holding companies from realizing the sums substantially in excess of book value when obtainable." (Comm. Br., p. 59).

But if we assume that the first quotation above is the one which the Commission really means, it still constitutes no reply to Electric's argument. Electric's argument was directed to the relationship between the evils to be remedied, the person responsible for those evils, the remedy to be applied, and the person to whom the remedy is applicable. The Commission's argument is directed to the different question of difficulty of administration.

Moreover, and again assuming that the first quotation above is the one which the Commission really means, the difficulties of bringing Electric's system into conformity with the standards of Section 11 so that Bond and Share's control may be severed, are substantially the same as the difficulties of bringing Electric's system into conformity with the standards of Section 11 for dissolution and distribution purposes.

II.

The Commission's disregard of Section 11(b)(1).

At no point in its brief does the Commission indicate a recognition of the affirmative mandate of Section 11(b)(1) with respect to integration. It certainly does not purport to be integrating the Bond and Share system, and it flatly denies any duty to integrate the Electric system, at least through Electric.

As in its opinion, so in its brief, the Commission disposes of the integration of Electric's southern system, without any hearing, in terms of doubt and conjecture as to whether Electric is entitled to retain that system.* (Comm. Br., pp. 30-31, 130-2).

Moreover, the brief of the Commission is plainly misleading in so far as Electric is concerned, when it says:

> "Further evidence that the subholding companies were not designed to coordinate or supervise the activities of their operating company subsidiaries is found in their geographic grouping. An examination of Appendices B and C attached to this brief shows that American's subsidiaries are scattered from Florida to Washington and from Minnesota to Texas. Those of Electric are similarly dispersed from Mississippi to Oregon. *From an operational point of view no conceivable plan for coordination can be found in the grouping of these companies*

* Contrary to the statement at page 131-n of the Commission's brief, a "careful reading" of Electric's main brief indicates that it *has* abandoned its contention that the United Gas properties may be retained with its southern system. Indeed, on November 6, 1945, Electric filed with the Commission a plan for distributing its holdings of United Gas stock to Electric's preferred stockholders.

> *under their subholding companies,* and, as we have seen, their actual management ignores these lines." (Comm. Br., pp. 85-86).

The italicized portion of the foregoing quotation cannot possibly apply to Electric's southern system. An examination of the map constituting Appendix B to the Commission's brief or of the map constituting Appendix C to Electric's main brief discloses that Electric is a holding company holding together what is at least an interconnected system and *prima facie* an integrated system.*

Much of the Commission's discussion with respect to Electric's right to retain its southern electric system is directed to the argument that Electric has not performed any "functions" with respect to that system in the past. Electric contends that past activities are irrelevant to the integrating and simplifying tasks of the Commission under Section 11(b)(1), as the Commission itself agrees:

> "* * * our examination of the record convinces us that claims of past benefits have not been established *or are irrelevant* * * *." (R., Vol. II, 612)

Moreover, it is to be expected that so long as Electric's subsidiaries are in the Bond and Share system, most holding company functions would be performed by Bond and Share. Section 11(b)(1), however, must contemplate changes in the specific functions of particular holding companies as their systems are integrated by the Commission.

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* Compare the statement at page 132 of the Commission's brief with respect to the investment of Electric in its four electric subsidiaries comprising its southern system:

> "Since the Commission did not pass upon these questions, it was not inconceivable, at least in the case of Electric, that petitioners might ultimately be transformed into appropriate corporate vehicles for holding under common control integrated public utility systems."

The question is not what holding company functions Electric has performed in the past, but instead what holding company functions it will perform in the future with respect to the integrated system which it may be permitted to retain. It is sufficient to establish Electric's status under Section 11(b)(1) that Electric does own an interconnected electric system which is, or is at least capable of being, fully integrated, and that Electric is preponderantly owned by the public.

If the Commission may completely disregard the provisions of Section 11(b)(1) merely by claiming to act pursuant to Section 11(b)(2), Section 11(b)(1) may be rendered a nullity. As set forth in Electric's main brief, the requirements of Section 11(b)(1) and the requirements of Section 11(b)(2) are coordinate, and simplification to the point of making integration impossible through the medium of existing holding companies is to deprive those holding companies of rights clearly accorded them in the statute. Electric's right to retain an integrated public utility holding company system can hardly be disposed of on the mere assertion by the Commission that Electric has not been demonstrated, without a hearing, to be "superior" to a new holding company formed for the purpose of integrating its southern system. (Comm. Br., p. 31).

The Commission contends that Electric's argument with respect to the coordinate purposes of Sections 11(b)(1) and 11(b)(2) can be reduced to the contention that dissolution can never be ordered under Section 11.* Electric made no

* "Petitioner's contention that the Commission must try to find an integrated system or combination thereof for each existing holding company in a holding company system is only another way of arguing that dissolution of a useless holding company is never permissible." (Comm. Br., p. 136).

such contention, and specifically so stated. (Electric Br., pp. 2, 12). The Commission's brief, however, can, indeed, be reduced to the converse contention, namely, that Section 11 authorizes the Commission, at its mere whim, to dissolve virtually all holding companies.* Any such construction of Section 11(b)(2) is clearly untenable.

The Commission's brief also disparages the plan filed by Electric, in the same terms used in the findings and opinion. Even the brief, however, does not contend that the plan is frivolous. Indeed, an examination of the plan (R., Vol. II, 487) shows that it provides for action far too drastic with respect to both the properties and the securities of Electric to be termed frivolous. The fact that all questions under both Sections 11(b)(1) and 11(b)(2) were not fully provided for in the plan must be considered in connection with the time when the plan was prepared and filed. In 1941, most of the reorganization problems which have since been settled, at least so far as the Commission is concerned, and to some extent by the courts, were then completely unresolved.

The plan was prepared and filed in good faith for the purpose of bringing Electric and its system into conformity with the integration and corporate simplification provisions of Section 11. Electric made a good faith effort to secure a hearing on the plan by moving for the consolidation of the plan proceedings with what had by then become known as the "dissolution proceedings." If the plan has not become effective, that is due to the fact that the Commission denied the consolidation motion and entered a

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* "The process of simplification may well result in the elimination of all existing holding companies in a system because a new company is more suitable for the purpose of holding the system together than any of the existing holding companies." (Comm. Br., p. 136).

dissolution order instead, and not because of any inherent weakness in the plan itself.*

The attempt in the Commission's brief (p. 32) to infer that this plan for full compliance with Section 11 by Electric was "merely litigation strategy" and to bolster this assertion by referring to subsequent action on the part of Electric to bring it into conformity with the provisions of Section 11 (Comm. Br., pp. 32, 140), is entirely without foundation.

III.

The Commission's entanglement in its own figures.

The Commission is at great pains in its brief (pp. 46-62) to attempt to extricate itself from the difficulties which result from the inaccuracies and guess-work underlying the figures on which it bases its dissolution order.

Electric's argument was to this effect (Electric Br., pp. 39-42): the Commission's conclusion that "the continued existence and capital structure of Electric unfairly and inequitably distribute voting power among security holders of the Bond and Share system" was based (*a*) upon a finding that voting power was unfairly and inequitably distributed among the security holders of the Electric system, and (*b*) upon a finding that voting power was unfairly and in-

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* The court below referred to Electric's plan as having been "tardily filed" (R., Vol. IV, 879). This is an unfair statement, particularly in view of the fact that the Commission did not conclude the dissolution proceedings or deny the motion to consolidate the plan proceedings with the dissolution proceedings until 8½ months after the plan was filed and the motion made. Whether or not this 8½ months' delay on the part of the Commission was pursuant to an understanding with counsel for Electric, as asserted by the Commission (Comm. Br., p. 137-n), is not relevant to the question of whether the plan was "tardily" filed.

equitably distributed among the security holders of the Bond and Share system, including Electric (R., Vol. II, 624). The conclusion was expressly based upon *both* of these findings.

These findings in turn were based upon "the foregoing figures"—which include an interest of Electric in its subsidiaries equal to 39%, "adjusted" to 32%, and further "adjusted" to 15.65% (R., Vol. II, 622-624). The findings were expressly based upon *all* these figures.

We do not argue, as the Commission says, that the opinion is based "solely" on the 15% figure. (Comm. Br., pp. 47-48). We do point out that the Commission itself based its decision on all three of the "foregoing figures." And we point out in addition that the 39% and the 32% figures give the Commission no real support for its decision. It has uniformly and without discussion accepted a 25% common stock equity as a sufficient investment to support voting control. The following are decisions supporting the 25% investment, which have come down in recent weeks:

Matter of Northern Indiana Public Service Company, SEC Holding Company Act Release No. 6149, p. 3, footnote 2 (October 22, 1945);

Matter of Pennsylvania Power Company, SEC Holding Company Act Release No. 6140, pp. 6-7 (October 17, 1945);

Matter of Union Electric Company of Missouri, SEC Holding Company Act Release No. 6134, p. 9 (October 16, 1945);

Matter of Columbia Gas & Electric Corporation, SEC Holding Company Act Release No. 6132, p. 7 (October 15, 1945);

Matter of Florida Power Corporation, SEC Holding Company Act Release No. 6124, p. 14 (October 11, 1945).

The Commission says that it placed greatest emphasis on the figures before adjustment for write-ups and depreciation because, it states, "those are the figures mentioned immediately before the Commission's conclusion that 'on the basis of the foregoing figures,' voting power was unfairly and inequitably distributed." (Comm. Br., p. 48). Aside from the fact that the last figure regarding Electric's investment in its subsidiaries, prior to the phrase "on the basis of the foregoing figures," is the 15% fully "adjusted" equity, the fact is that nothing in the decision of the Commission indicates that it relied upon one set of figures any more than another.

The Commission says that it was not dealing in assumptions and guesses with respect to these figures. (Comm. Br., p. 56). The very language of the Commission's opinion (R., Vol. II, 623), however, refutes this. There is no conclusive or definitive language on the entire page where the figures are dealt with. The language used is: "apparent system write-up," "it appears," "indicates," "may be necessary," "probable," "for present purposes," "would represent," etc. And indeed, further on in the opinion (*id.* 646) the Commission discloses its then state of mind concerning the entire question, by stating that

> "there likewise exist *substantial questions* as to the equity of American and Electric in many of the subsidiaries which they claim as important parts of their systems; *if it should later be determined* that little or no equity exists in certain such companies, they of course would not be retainable apart from the standards of Section 11(b)(1)."

The Commission's arithmetical error in treating an alleged zero as though it were a negative figure of $28,000,000 (Electric Br., p. 42) is not explained away by the foot-

note in the Commission's brief (pp. 53-54). Whether the addition of a column of figures is for the purpose of determining "system investment," "equity evaluation" or plain grammar-school arithmetic, a zero does not become a negative figure.

The unusual character of these basic figures in the Commission's decision can only be explained as the result of its zealous search for what it terms "the smallest possible equity of Electric in the capitalization of its subsidiaries" (R., Vol. II, 623).*

The figures cited to the Court at pages 39 to 42 of Electric's main brief, representing the actual determinations by the Commission with respect to Electric's investment in certain of its subsidiaries, still stand.** The Commission's

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* The Commission's brief seeks to imply that Electric failed to object to the figures in Appendix F-2 to the Commission's opinion and that these figures constitute part of an agreed statement of facts upon which the case comes up. (Comm. Br., pp. 35-36, 56). Actually, Electric did object most strenuously to the figures now complained of, in conference with the staff. Aside from that, however, the figures in question do not purport to be "findings." The point for review here is not whether the figures are correct assumptions or guesses; but whether the Commission may base its decision upon assumptions and guesses. Electric reserved its right to full review of any such questions (R., Vol. II, 522).

** A further example of the inaccuracy of the Commission's findings with respect to Electric's investment in its subsidiaries is furnished by a decision of the Commission which has come down since Electric filed its main brief. Electric's investment in Dallas Power & Light Company is shown in Appendix F-2 to the Commission's opinion (R., Vol. II, 667) at a book figure of $5,652,000. This is "adjusted" downward first to $4,686,000 and then to only $533,752. Yet this investment—which on the Commission's dissolution findings is presumably almost all water—was recently sold *to an affiliate* with the Commission's approval for $17,350,000. *Matter of American Power & Light Company, Texas Utilities Company and Electric Power & Light Corporation*, SEC Holding Company Act Release No. 6158 (October 24, 1945).

For the Court's assistance, we recapitulate in Appendix A to this brief the "findings" in Column (13) of Appendix F-2 and compare them with the Commission's subsequent definitive determinations.

brief has not succeeded in explaining away its error in computing Electric's investment in its subsidiaries, and the error is fatal to the order for the dissolution of Electric.

Conclusion.

The order of the United States Circuit Court of Appeals for the First Circuit should be reversed, with directions that the orders of the Securities and Exchange Commission issued August 22 and August 28, 1942, be set aside.

Respectfully submitted,

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Appendix A.

Tabulation showing disparity between the findings upon which the dissolution order is based and subsequent definitive determinations with respect to 6 out of 11 subsidiaries of Electric which are shown in Appendix F-2 and as to which the comparisons are possible.

	Electric's equity in its subsidiaries as shown in Column (12) of Appendix F-2	Commission's definitive determination of Electric's equity in its subsidiaries or approved sale price of such equity
Dallas Power & Light	$ 533,752	$ 17,350,000*
Idaho Power Company	5,603,794	9,929,000
Louisiana Power & Light	181,841	6,815,000
Mississippi Power & Light	114,999	2,500,000
United Gas Corporation	60,460,109	101,081,010
Utah Power & Light	*(28,059,794)*†	—
Totals	$38,834,701	$137,675,010

* Approved sale price.

† Improperly treated as algebraic negative figure. See Electric's main brief, p. 42.